

**BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA**

Order Instituting Rulemaking on the  
Commission's own motion for the purpose of  
considering policies and rules governing utility  
construction contracting processes

FILED  
PUBLIC UTILITIES COMMISSION  
September 4, 2003  
SAN FRANCISCO OFFICE  
RULEMAKING 03-09-006

**ORDER INSTITUTING RULEMAKING**

**Summary**

By this order, we initiate an Order Instituting Rulemaking on our own motion into the current practices of utility construction contracting processes and possible future rules governing those contracting processes.

We have two goals in this rulemaking. First, we seek to develop an understanding of the construction contracting processes of the electric, natural gas, telecommunication and water utilities – the criteria by which utilities' contract awards are based, the overall magnitude of the utilities' annual construction contracts granted, the processes used by utilities to solicit and award construction contracts, and their policies regarding the execution of primary contracts and subcontractor agreements. Second, we will consider adopting rules to ensure that utility construction contracting practices are consistent with rules governing state and federal public works contracting practices. We seek comment on both of these issues.

**Background**

The Commission currently does not impose specific requirements on our jurisdictional utilities regarding their solicitation and awarding of bids for

construction of utility facilities. However, state law imposes certain requirements on state entities bidding out public works projects, as well as on the prime and subcontractor bidders of such projects. The purpose of these requirements is to avoid the practice known as “bid shopping” or “bid peddling”, which occurs when prime contractors ask, require or otherwise influence subcontractors to lower bids for subcontract work after the prime contract is awarded. In such situations, the government entity is, essentially, not getting what it paid for. To prevent such actions, California Public Contract Code Section 4100 requires that prime contractors provide detailed information to the public contracting entity, subject to a specific threshold subcontracting amount, about “any subcontractor who will perform work or labor or render service to the prime contractor” in connection with a public improvement project. It also prohibits successful prime contractors from substituting a person as a subcontractor in place of the subcontractor listed in the original bid, with certain exceptions. The Legislature noted in adopting these requirements that

“...the practices of bid shopping and bid peddling in connection with the construction, alteration, and repair of public improvements often results in poor quality of material and workmanship to the detriment of the public, deprive the public of the full benefits of fair competition among prime contractors and subcontractors, and lead to insolvencies, loss of wages to employees, and other evils.”  
(California Public Contract Code Section 4101.)

We note further that presently there is pending in Congress a bill, H.R. 1348, that addresses substantially the same issue. H.R. 1348 requires that each invitation to bid, or request for proposal issued by the federal government for construction contracts of \$1 million or more, include language explicitly prohibiting the practice of bid shopping. In addition to the form of bid shopping

described above, H.R. 1348 addresses a bidding process known as “reverse auctions. Reverse auctions are an emerging internet trend for buying goods and services, in which contractors submit continuing anonymous bids against one-another in real time in an effort to win the lowest price. Each bidder is asked to submit its price at a specific time at which time the lowest of the bids is listed. All other bidders are then given the opportunity to revise their bids to be below the current low bid. This process continues until there are no additional revised bids. Language in H.R. 1348 appears intended to prohibit reverse auctions for federal public improvements, by defining bid shopping as occurring not only when a contractor shops around a subcontractor’s bid, but also when the awarding federal entity discloses a competitive bid in order to obtain a lower primary contractor’s bid.

## **Discussion**

Many prohibitions on construction bid shopping are intended to assure quality and best value with respect to Federal construction projects. Bid shopping and reverse auction processes create a disparity between a project’s costs and its value if costs are cut below the cost to the contractor during the bidding process, or if the primary contractor reduces project materials, labor or quality after a contract is awarded. In such situations, bid shopping can result in increased change orders, higher maintenance costs, and lower overall value to the project beneficiary. On the other hand, a reverse auction process also may provide certain benefits in the form of driving down prices for certain types of commercial commodities, and providing owners or contracting entities with an innovative means of soliciting bids. We seek here to understand whether it is appropriate in all circumstances. Reverse auctions can represent a bid-

solicitation and award process weighted solely – or at least primarily – on cost. Clearly, a utility construction contract procurement process that keeps costs low provides benefit to the utility’s ratepayers. In the context of public utility projects or facilities designed to meet the health, safety and reliability needs of California’s utility consumers, however, other variables such as worker safety, product safety, product quality and timeliness of project completion all must be considered as well.

As a preliminary matter, therefore, we initiate this Order Instituting Rulemaking in order to gain a greater understanding of the bid shopping practices that the state law and draft federal legislation described above are designed to avoid for public improvement improvements projects, and to gather information about our jurisdictional utilities’ construction contracting practices. We intend to gather information about the utilities’ construction contracting bidding practices, whether they are currently engaging in bid shopping practices, the outcomes of construction award practices, and the magnitude of utility construction contracts. That information will allow us to consider new rules, if necessary or appropriate, that ensure utility construction contracting processes are consistent with requirements that apply to state public improvements projects and provide the best construction outcome for California’s utility customers.

### **Preliminary Scoping Memo**

This rulemaking will be conducted in accordance with Article 2.5 of the Commission’s Rules of Practice and Procedure. As required by Rule 6 (c)(2), this order includes a preliminary scoping memo as set forth below.

In this proceeding we will consider the issues raised above in the body of this order. To that end, the first phase of this proceeding will focus on gathering the facts about the current construction contracting practices of the respondent utilities. We direct each of the respondents to this rulemaking to file a report according to the schedule outlined below, detailing the utility's answers to the following questions.

1. What are the utility's construction contracting practices currently? Identify the processes used to solicit, consider and award construction contracts.
2. Do the utility's construction contracting practices include any form of bid shopping as described above? If so, please articulate the methods used.
3. Identify all construction contract awards by project and contract award amount for the last five years.
4. Explain the criteria by which the utility's contract awards are based.
5. Should the potential rules considered in this rulemaking apply to utilities that meet a certain threshold, such as utility size, or construction budget? If so, how should that threshold be defined, and at what level?

This information will allow us to consider in a subsequent phase adopting rules to ensure that utility construction contracting practices are consistent with rules governing state and federal public works contracting practices.

Pursuant to Rule 6(c)(2), we preliminarily determine the category of this rulemaking proceeding to be quasi-legislative as the term is defined in Rule 5(d). It is contemplated that this proceeding shall be conducted through a written record and that an order will issue on the merits based on the pleadings timely

filed in this docket. However, parties will have the opportunity to comment on the necessity of hearings, and we may re-evaluate both the categorization and need for hearings after review of the comments.

In accordance with Rules 6.3 and 6(c)(2), the proposed schedule is as follows:

Rulemaking Issued	September 4, 2003
Utilities File Report	October 24, 2003
Opening Comments (Including responses to order)	November 21, 2003

As set forth in the schedule above, the utilities named as respondents to this proceeding should file and serve their report before interested parties (which may include the same utilities) file their comments (including any response to this order). Following review of the utilities' reports and interested parties' opening comments, the assigned ALJ shall convene a prehearing conference to discuss the issues, scope, and schedule of this proceeding. After the prehearing conference, the Assigned Commissioner will issue a scoping memo that finalizes the category, scope, and schedule of this proceeding. (See Rules 6(c)(2) and 6.3.) After the scoping memo issues, parties may file and serve an appeal to the Commission regarding the ruling on category. (See Rule 6.4.)

Consistent with Rule 6(e), we expect that this proceeding will be concluded within 18 months.

Any person interested in participating in this rulemaking who is unfamiliar with the Commission's procedures should contact the Commission's

Public Advisor's Office in San Francisco at (415) 703-2074 or in Los Angeles at (213) 649-4782.

**Service of This Order and Service List for This Proceeding**

All natural gas, electric, telephone and water utilities under the Commission's jurisdiction and their Commission-regulated subsidiaries and affiliates are named as respondents to this order. We direct that these utilities shall be served with this order.

This order should also be served on the services list for Rulemaking R.03-02-035, the rulemaking to consider amendments to General Order 156, utility procurement and contracting from Women, Minority and Disabled Veteran Business Enterprises.

Being served with this order does not guarantee that you will be placed on the rulemaking's service list. Respondent utilities shall be placed on the service list by the Process Office.

Anyone else wishing to be placed on the service list for this rulemaking should submit his or her request within 20 days of the mailing date of this order to the Commission's Process Office, 505 Van Ness Avenue, San Francisco, California 94102. Parties should reference this rulemaking number and indicate whether they wish to be on the service list for this proceeding and, if so, if they wish to be an appearance, state service or information only. (An appearance means that the party will actively participate in this rulemaking by filing comments, etc. See description of state service and information only below.) These parties should also include their name, the name of their representative (if any), their address, and telephone and facsimile numbers, and an e-mail address,

unless the party states that no e-mail address is available. A service list will then be prepared and posted on the Commission's web site at [www.cpuc.ca.gov](http://www.cpuc.ca.gov) as soon as practicable. Requests to be included in the service list made more than 20 days of this order's mailing must be sent to and approved by the assigned ALJ.

Those persons employed by the State of California who are interested in this proceeding may be added to the "state service" section of the service list either by appearing at the prehearing conference and filling out an appearance form, or they may mail a written request to the Process Office within 20 days of this order's mailing. All of the names that appear on the state service list shall be served with all documents that parties may submit or file in connection with this proceeding.

Those persons who do not want to be parties, and only want notice of the hearings, rulings, proposed decisions, and decisions, may either appear at the prehearing conference and fill out an appearance form, or they may mail a written request to the Process Office requesting that they be added to the service list for information only.

The assigned commissioner for this proceeding is Loretta Lynch.

### **Ex Parte Communications**

This proceeding is subject to Rule 7 which specifies standards for engaging in ex parte communications and the reporting of such communications. Pursuant to Rules 7(a)(4) and 7(d), ex parte communications will be allowed in this proceeding without any restrictions or reporting requirements until the assigned Commissioner makes an appealable determination of category.

Following the Commissioner's determination, the applicable ex parte communications and reporting requirements shall depend on such determination unless and until the determination is modified by the Commission pursuant to Rules 6.4 and 6.5.

Therefore, **IT IS ORDERED** that:

A rulemaking is instituted on the Commission's own motion into the current practices of utility construction contracting processes and possible future rules governing those contracting processes.

1. The Executive Director shall cause this Order Instituting Rulemaking (OIR) to be served on:

- a. The jurisdictional natural gas, electricity, telecommunications and water utilities;
- b. The service list for Rulemaking R.03-02-035, the rulemaking to consider amendments to General Order 156, utility procurement and contracting from Women, Minority and Disabled Veteran Enterprises.

2. The assigned administrative law judge (ALJ) shall establish the initial service list for this proceeding by ruling on or before twenty-one (21) days after this order is mailed. By close of business fourteen (14) days after this order is mailed, any person or entity that seeks:

- a. "Appearance" status in order to participate as a party in this proceeding shall contact the Commission's Process Office by FAX (415/703-2823) or e-mail (ALJ\_Process@cpuc.ca.gov) and submit the information required for the service list (name & organization represented, if any; address; telephone number; fax number; e-mail address, if available).
- b. Non-party status in the "State service" or "Information only" category, as applicable, shall contact the Commission's Process

Office by FAX (415/703-2823) or e-mail  
(ALJ\_Process@cpuc.ca.gov) and submit the same information.

3. The category of this rulemaking is preliminarily determined to be “quasi-legislative” as that term is defined in Rule 5(d) of the Commission’s Rules of Practice and Procedure.

4. The preliminary schedule for this rulemaking is set forth herein. The assigned ALJ or the Assigned Commissioner may change the dates. All comments shall be filed with the Commission’s Docket Office in paper form as described in Article 2 of the Commission’s Rules of Practice and Procedure.

5. Any party listed in the “Appearances” category on the service list that provides an e-mail address shall serve and receive all pleadings by e-mail in Microsoft Word format. There is no need to serve hard copies of the pleadings on any party listed in the Appearances and State Service categories on the service list if that party has provided an e-mail address. If a party in the Appearance or State Service categories has not provided an e-mail address, then that party must be served with a hard copy.

6. Any party who objects to the preliminary categorization of this rulemaking or the preliminary schedule shall file an objection in its opening comments.

This order is effective today.

Dated September 4, 2003, at San Francisco, California.

CARL W. WOOD  
LORETTA M. LYNCH  
GEOFFREY F. BROWN  
SUSAN P. KENNEDY  
Commissioners

R.03-09-006 COM/LYN/epg

I abstain.

/s/ MICHAEL R. PEEVEY  
President